

Nationwide produces this publication to provide public defined contribution plan sponsors with information about federal legislative and regulatory activity that may be relevant to plan administration and/or design.

Federal Legislative and Regulatory Report

April 2004

I. Washington Update – Lifetime Savings Account Legislation Introduced

Congress is beginning its spring recess and will be out of session through April 16th.

On March 31, 2004, Senator Craig Thomas (R-WY) and Representative Sam Johnson (R-TX) introduced legislation to create Lifetime Savings Accounts (LSAs). This legislation is H.R. 4078 and S. 2263 and is called the “Lifetime Savings Accounts Act of 2004.” There were 22 co-sponsors of the bill in the House, including five Republican members of the House Ways and Means Committee. This may be an indication of the interest there will be to bring this proposal back next year (2005) if it fails to be enacted in 2004.

This proposal closely tracks the 2005 President’s Budget proposal on LSAs, which proposed to allow individuals to make annual after-tax contributions of up to \$5,000 to an LSA regardless of income, age or eligibility requirements. Distributions would be tax-free and could be made at any time, for any reason. Education savings accounts and qualified tuition programs under section 529(c)(3)(E) could be rolled into LSAs. This legislative package does not include provisions relating to Retirement Savings Accounts (RSAs) or Employer Retirement Savings Accounts (ERSAs).

The [table on page 4](#) summarizes the major provisions of this Act. For more information, go to <http://thomas.loc.gov> and enter H. R. 4078.

Representatives Portman and Cardin continue to work on their next retirement bill. The earliest that it is anticipated to be released is May. There continues to be discussions about including a provision in this legislation to make the saver’s credit fully refundable and applying the credit automatically to an employer-sponsored retirement plan account or other retirement savings vehicle.

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II. 403(b) Plans for State Employees

Representative Virgil Goode introduced H.R. 3718, a bill that would permit state government employers to establish and contribute to section 403(b) plans. The bill has been referred to the House Ways and Means Committee for further study.

For more information, go to <http://thomas.loc.gov> and enter H. R. 3718. Since the passage of EGTRRA, Section 403(b) plans have generated a lot of interest because:

- 403(b) and 457(b) deferrals no longer are coordinated, permitting participants in both of these plans to defer twice the annual maximum limit or \$26,000 for 2004. Separate catch-up amounts may also be available providing for additional deferrals for eligible participants.
- 403(b) plan sponsors may contribute accumulated unused sick and vacation pay for terminated participants, up to \$41,000 (indexed) per year for five years for a maximum contribution of \$205,000.

Currently, 403(b) plans may be sponsored only by 501(c)(3) private sector tax-exempt organizations, such educational, religious and charitable organizations and public schools and universities.

III. Temporary Relief for Defined Benefit Plans

On April 2, 2004, the House passed the Pension Funding Equity Act of 2004 (H.R. 3108) which would temporarily replace the current outdated 30-year Treasury bond interest rate with a long term corporate bond rate through 2005. Although the Treasury no longer issues 30-year Treasury securities, private sector employers still use this rate, which the IRS publishes monthly, to calculate their defined benefit plan contributions and liabilities.

The goal in switching from the 30-year Treasury bond rate to a long term corporate interest rate is to help plans that were adequately funded before the stock market decline to meet large increases in funding costs resulting from recent poor investment performance. The Senate is expected consider this measure shortly. Once a temporary relief is enacted, lawmakers will begin work on a permanent solution.

For more information about Pension Funding Equity Act of 2004 (H.R. 3108), go to <http://edworkforce.house.gov/issues/108th/workforce/pension/stateofman.pdf> and <http://waysandmeans.house.gov/News.asp?FormMode=print&ID=191>

IV. More HSA Guidance Issued

On March 30, 2004, the IRS issued four additional pieces to the Health Savings Account (HSA) guidance. To be eligible to make contributions to HSA, individuals must:

- Be covered under a High Deductible Health Plan (HDHP)
- Not be covered under non HDHP plan, except for certain types of permitted coverage such as dental and vision, worker's compensation, property and casualty insurance
- Not be eligible for Medicare (Age 65)



The annual HDHP deductible is \$1,000 for single coverage and \$2,000 for family coverage. Generally, HSAs may not reimburse expenses incurred prior to the HSA's establishment or before the HDHP deductible is met. The tight timeframes between the enactment of the Medicare Reform Act, which created HSAs in December 2003, and their availability beginning January 1, 2004 have proved problematic.

Many employers and health plans did not have sufficient time to modify their 2004 health plans to conform to the statutory HDHP requirements. Also, many individuals who are eligible for HSAs have not been able to find HSA trustees or custodians to set them up.

As a result of timing and clarification issues, the IRS has issued guidance to temporarily suspend certain HSA contribution and distribution requirements, define safe harbors for preventive care, and address prescription drug coverage outside of an HDHP.

We have provided a [table outlining the IRS' guidance](#), beginning on page 5.

On April 7, 2004, the **Department of Labor issued its guidance** on HSAs. Among other details, it outlined the extent to which they will be considered welfare plans governed by the Employee Retirement Income Security Act (ERISA). The Field Assistance Bulletin (FAB) from the U.S. Department of Labor's (DoL) Employee Benefits Security Administration (EBSA) indicated that, while private-sector employer-sponsored High Deductible Health Plan (HDHP)s are group health plans subject to ERISA's reporting, disclosure, fiduciary responsibility and other requirements, HSAs generally will not constitute ERISA-covered plans. The FAB is located online at http://www.dol.gov/ebsa/regs/fab_2004-1.html.

Additional HSA guidance is expected later this summer. Also, previously published information from Nationwide® can be found in the December 2003, February and March 2004 editions of the *Federal Legislative and Regulatory Report*. Go to www.nrsforu.com and select the Employer tab. The link to the Reports may be found about halfway down the page.

IV. Keeping watch

Nationwide continues to monitor investigations into mutual-fund trading practices and related issues. The most recent information on these issues is on the Employer page of your plan Web site.

In addition, we report guidance on legislative and regulatory activity that is relevant to government sector defined contribution plans through our quarterly *Plan Sponsor Voice* newsletter, monthly *Federal Legislative and Regulatory Reports* and e-mail alerts distributed as needed.

Summary of the proposed “Lifetime Savings Account Act of 2004”	
Effective Date	LSAs will be available on or after January 1, 2005.
Description	An LSA is new type of individually owned account that is funded with after tax contributions and has no wage, age or distribution limitations. Money can be withdrawn at anytime for any reason.
Trust and Trustee Requirements	LSA money is held in a trust created for the exclusive benefit of the individual or his/her beneficiaries. LSA trustee must be a bank or IRS approved non-bank trustee. Custodial account or annuity contract issued by an insurance company qualified to do business in a State will be treated as a trust for these purposes. LSA trustees are required to provide accountholders and the IRS with annual reports. Failure to provide annual reports will be subject to penalties that apply to IRAs.
Contributions and Investments	Contributions must be in cash with after-tax money and may not be invested in life insurance contracts or co-mingled with other property except in a common trust fund or common investment fund. Maximum contribution, except for rollover contributions for any calendar year is \$5,000 a year (indexed to inflation after 2005) for all LSAs held in an individual's name.
Excess contributions	Will be subject to a 6% excise tax unless returned to accountholder prior to July 1 of the year following the year contribution is made
Distributions	Tax-free
Online sources for information	http://www.treas.gov/press/releases/js1280.htm http://thomas.loc.gov/ , select H.R. 4078 and S. 2263 http://www.americanbenefitscouncil.org/documents/lifetimesavings_thomas.pdf



IRS Guidance on HSAs

Guidance	Purpose of Guidance	Comments
IRS Notice 2004-25	<p>Temporarily suspends the requirement that HSAs can pay or reimburse only qualified medical expenses incurred after the establishment of the HSA.</p> <p>HSAs established or before April 15, 2005 for the 2004 calendar year may pay or reimburse on a tax-free basis medical expenses incurred on or after January 1, 2004, or the first day of the first month the employee becomes eligible to establish an HSA.</p>	<p>This relief will not be extended for HSAs established for calendar years 2005 and later.</p>
IRS Notice 2004-23	<p>Provides a safe harbor definition for preventive care benefits that may be offered under and HDHP without satisfying the HDHPs minimum deductible amounts such as:</p> <ul style="list-style-type: none"> ▪ Periodic health evaluations including diagnostic procedures ordered in connection with routine examinations such as annual physicals ▪ Routine prenatal and well-child care ▪ Child and adult Immunizations ▪ Tobacco cessation programs ▪ Obesity weight-loss programs ▪ Screening services for preventive care such as cancer screening, heart and vascular diseases screening, infectious diseases screening, and mental health conditions and substance abuse screening <p>Preventive care doe not include tests for existing medical conditions.</p>	<p>Generally an HDHP may not provide benefits for any year until the HDHP deductible for the year has been satisfied except for preventive care services, which were not defined in the original statute.</p> <p>Interaction with State Law Health Care Requirements</p> <p>State insurance laws often require health plans to provide certain health care benefits without a deductible or with a minimal deductible.</p> <p>This Notice states that for HSA purposes, the standards used in this IRS Notice and other IRS guidance will determine what qualifies as preventive care for HDHP purposes regardless of state law.</p> <p>The IRS continues to seek comments concerning additional standards for preventive care including:</p> <ul style="list-style-type: none"> ▪ Benefits or services that should be added ▪ Employee assistance, mental health or wellness programs ▪ Use of drug treatments

IRS Guidance on HSAs		
Guidance	Purpose of Guidance	Comments
IRS Revenue Ruling 2004-38	<p>This ruling states that individuals covered by both an HDHP that does not provide prescription drug benefits and a separate plan or rider (non-HDHP) that provide prescription drug benefits</p> <ul style="list-style-type: none"> May not contribute to an HSA if the prescription drug plan pays or reimburses the cost of prescription drugs before the individual has met the minimum annual deductible required under the HDHP <p>Example from the Ruling: An individual is covered under an HDHP, which does not provide a prescription drug benefit and is also is covered under another plan (or rider) that provides prescription drug benefits with no deductible but requires a co-payment for each prescription.</p> <p>Conclusion: This individual may not make HSA contributions because his/her HDHP does not provide prescription drug coverage and the separate drug plan or rider pays benefits before the minimum annual HDHP deductible is paid.</p> <p>Note: This restriction is suspended until January 1, 2006. See Revenue Procedure 2004-22 (below).</p>	<p>If a separate prescription drug plan or rider does not provide benefits until the minimum annual deductible of the HDHP has been satisfied or the prescription drug plan is part of an HDHP and subject to the minimum annual deductible, eligible individuals could make HSA contributions.</p>
IRS Revenue Procedure 2004-22	<p>Provides transition relief from Revenue Ruling 2004-38 (above).</p> <p>Until January 1, 2006 individuals covered by both an HDHP and a separate plan or rider that pays prescription drug benefits before the minimum annual deductible of the HDHP is met may contribute to an HSA.</p>	<p>This transition relief will not be available on or after January 1, 2006.</p>

